



June 20, 2007

To the Honorable Mayor, the Redmond City Council, and Citizens of Redmond, Washington:

The Comprehensive Annual Financial Report of the City of Redmond for the fiscal year ended December 31, 2006, is submitted herewith. This report is published to comply with State law (RCW 43.09.230) requiring annual reports for Washington municipal governments to be certified and filed with the State Auditor's Office within 150 days after the close of each fiscal year.

Responsibility for both the accuracy of the data, and the completeness and fairness of the presentation, including all disclosures, rests with City management. The City operates under a system of accounting internal controls that are concerned with the safeguarding of assets and the reliability of financial records. The definition of accounting control assumes reasonable, but not absolute, assurance that the objectives expressed in it will be accomplished by the system. The concept of reasonable assurance recognizes that the cost of internal control should not exceed the benefits expected to be derived.

Cities and counties of the State of Washington must comply with the Budgeting, Accounting and Reporting System (BARS) prescribed by the Office of the State Auditor. State law also provides for an annual independent audit by the Office of the State Auditor.

As a recipient of federal, state, and county financial assistance the City is required to undergo an annual single audit in conformity with the provisions of the Single Audit Act Amendments of 1996, Budget Circular A-133, *Audits of State and Local Governments*, and the March 2006 Compliance Supplement. This audit is conducted by the State Auditor's Office in conjunction with the City's annual independent audit. The results of the City's single annual audit for the fiscal year ended December 31, 2006 provided no instances of material weaknesses in the internal control structure or significant violations of applicable laws and regulations.

GAAP requires that management provide a narrative introduction, overview and analysis to accompany the basic financial statements in the form of *Management's Discussion and Analysis (MD&A)*. This letter of transmittal is designed to complement the MD&A and should be read in conjunction with it. The City of

Redmond's MD&A can be found immediately following the independent auditor's report.

Profile of the Government

Incorporated in 1912, Redmond is the sixteenth largest city in the state of Washington encompassing an area of 16.94 square miles east of downtown Seattle on the east side of Lake Washington. Redmond has grown from a population of 1,453 in 1960 to a 2006 population of 49,890.

Redmond is a non-charter code city, operating under Section 35A of the Revised Code of Washington. It has a Mayor/Council form of government. The Mayor and the seven member City Council are elected for staggered four-year terms and are elected at-large, rather than by district. Members of the City Council are responsible for establishing the general direction and policies for the City and for providing the resources necessary to carry out those policies. As the City's chief administrator, the Mayor is responsible for carrying out the policy and direction set by the City Council. This includes the enforcement of laws and ordinances, the execution of contracts and agreements, and maintenance of peace and order in the City.

The City of Redmond provides a full range of municipal services, including police and fire, emergency medical services, planning and zoning, street maintenance and construction, parks and recreation, and general administrative services. The City operates enterprise funds for water and wastewater services and stormwater management.

This report includes all funds, account groups, agencies, and boards and commissions that are controlled by, or dependent on, the City's executive and legislative departments. Included as part of the reporting entity are the Redmond Public Corporation and Redmond Community Properties. Additional information on these entities can be found in the Notes to the Financial Statements.

CITY OF REDMOND

The City prepares budgets on the modified accrual basis in accordance with the Revised Code of Washington (RCW) 35A.33. Biennial budgets must be adopted by the City Council prior to the first of each odd numbered calendar year. Reviews are conducted at mid-biennium and any changes for the second half of the biennium are adopted by the City Council.

The biennial budget serves as the foundation for the City of Redmond's financial planning and control. The budget is prepared by fund and department. A budget increase or decrease to a fund must be authorized by the City Council, while appropriation changes within a fund may be authorized by the Mayor. All budgets are controlled on a fund basis.

Local Economy

Redmond has evolved from a small town with logging and farming as its chief industries into a city of high tech and light manufacturing, business parks, and a large outdoor mall adjacent to the downtown retail core. The largest employer in Redmond is Microsoft with United Parcel Service, the Lake Washington School District, and Genie Industries also having a significant presence in the City.

Redmond's economy continued to rebound from the economic recession that began in 2001, albeit at a modest rate. Sales tax revenues, employment growth, and development activity all increased as the economy strengthened. For the first time in five years, sales tax revenues for 2006 were above sales tax revenues for 2000 led by sales in the retail and communications sectors. Employment growth in the Puget Sound region was 3.6% in 2006 with expected growth of 2.8% and 2.6%, respectively, in 2007 and 2008. Much of the employment growth in Redmond is led by Microsoft, adding 1,600 to 2,000 new jobs per year at its Redmond campus. Microsoft attracts other technology businesses to the area, contributing further to the employment growth. Development activity is also being pushed by Microsoft as they invest \$1 billion over the next three years adding 14 new buildings with 3.1 million square feet of office space. Microsoft has pledged \$35 million to support City infrastructure in conjunction with their development projects. Ongoing revenue from these projects to support City operations is not expected to be material. Two other significant projects in the downtown area are a large condominium development and a new Sound Transit center with an adjoining apartment complex scheduled to begin construction in 2007.

To ensure the City keeps abreast of and incorporates economic conditions into its financial plans, revenues are

projected for the next six years and the forecast is updated annually. Operating expenses are supported by ongoing revenues per City policy. From 2001 to 2006 significant cost cutting measures were implemented to keep City expenses in line with actual revenues, and this trend will continue into the next biennium.

Long-term Financial Planning and Relevant Financial Policies

In early 2006 the Redmond City Council adopted a 6-year financial plan to address existing service deficiencies. In line with the City's financial policy to maintain a diversified and stable revenue system, the financial strategy calls for increases in four revenue sources for 2006. Three of these revenue sources were increased by Council vote. The utility tax rate and the business license fee increased to ensure residents do not shoulder the entire burden of increased revenues. Developer fees increased to establish user fees at a level related to the cost of providing the service consistent with existing fiscal policies.

The fourth proposed revenue source, an increase in the property tax levy above the 1% maximum allowed by law, was rejected by the voters. The Council will pursue the property tax levy increase with the voters in 2007 to raise the revenues needed to fund some public safety needs and parks programs. Despite these revenue increases, services to the public are expected to continue to decline due to limited resources in the General Fund.

City financial policies restrict the use of borrowed funds to capital improvements that can't be financed from current revenues. Debt is not used for current operations.

Redmond is in a continuous process of both short-term and long-term financial planning. Short-term financial planning is inherent in the development of the City's biennial budget. Concurrent with the biennial budget, the City's long-term capital needs and potential funding sources are assessed. During each biennial budget planning process, initiatives for the next two years are identified. The budget is developed with the goal of attaining these initiatives.

Major Initiatives

The City received several awards for excellence in 2006 including a Davey, an international creative award, for design of the Focus on Redmond magazine and the Arts in the Parks brochure; a City Livability Award from the U.S. Conference of Mayors and Waste Management for its R-

Trip commute trip reduction program; and a Website Merit Award from the Washington Recreation and Parks Association for the City's tourism website.

Significant construction projects completed in 2006 ranged from well rehabilitation to playground equipment. The City embarked on a Water Source Improvement Project several years ago to completely renovate four of its five wells. Rehabilitation of Well 5 was completed in 2006. Property was acquired to move Wells 1 and 2 from Anderson Park and construction is scheduled to begin in the fall of 2007 or early spring of 2008. Well 3 is scheduled for rehabilitation beginning in the spring of 2007. Well 4 has been rehabilitated and is in operation. Park projects were completed in 2006 at Idylwood Beach Park with the addition of play equipment and at Hartman Park where new field turf and floodlights were installed. Land was acquired and work done to complete a missing section of the Bear Creek Trail and 3.5 acres of open space was acquired at Perrigo Heights.

Two successful ongoing community events were featured in 2006, Derby Days and Redmond Lights. Derby Days, held in mid-July, celebrates the 4th of July holiday and Redmond's bicycling heritage. Community events for the whole family include a carnival, a criterium bicycle race, children's parade, live music for all musical tastes, and family entertainment from jugglers to reptiles. Redmond Lights is the City's annual year-end holiday celebration, running from early December through early January. This event celebrates holiday traditions from many countries and features music, lights, children's crafts, and a food and toy drive.

Other initiatives of note in 2006 were the adoption of school impact fees to be collected by the City on behalf of the Lake Washington School District and the adoption of the North Redmond Neighborhood Plan by the City Council. Neighborhood plans provide guidelines for the infrastructure, public safety, design standards, growth, etc. of neighborhoods and are developed or updated with input from neighborhood citizen committees.

Awards and Acknowledgments

The Government Finance Officers Association of the United States and Canada (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to the City of Redmond for its Comprehensive Annual Financial Report for the fiscal year ended December 31, 2005. This was the twenty-first consecutive year that the government has achieved this prestigious award. In order to be awarded a Certificate of Achievement, a government

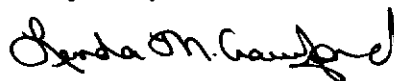
must publish an easily readable and efficiently organized comprehensive annual financial report. This report must satisfy both generally accepted accounting principles and applicable legal requirements.

A Certificate of Achievement is valid for a period of one year only. We believe our current comprehensive annual financial report continues to meet the Certificate of Achievement Program requirements and we are submitting it to the GFOA to determine its eligibility for another certificate.

The GFOA has also awarded the Distinguished Budget Presentation Award to the City of Redmond for its 2005-2006 biennial budget document. This is the first time in many years the City has submitted its budget to GFOA due to staff limitations in the City's Financial Planning Division. The GFOA gives this award to governments whose budget document meets the GFOA's criteria as an effective policy document, operations guide, financial plan, and communication device.

The preparation of the Comprehensive Annual Financial Report on a timely basis could not have been accomplished without the efforts and dedication of the staff of the Finance Department. I would like to express my appreciation to my staff and other personnel from various departments and agencies who assisted in its preparation. Also, I would like to thank the Mayor and the City Council for their continued interest and support in planning and conducting the financial operations of the City in a dedicated and responsible manner.

Respectfully submitted,



Lenda Crawford
Finance Director